

GENERAL INFORMATION

This document is an evaluation of the Community Reinvestment Act (CRA) performance of **McHenry State Bank, McHenry, Illinois** prepared by the **Federal Reserve Bank of Chicago**, the institution's supervisory agency.

The evaluation represents the agency's current assessment and rating of the institution's CRA performance based on an examination conducted as of **January 8, 1996**. It does not reflect any CRA-related activities that may have been initiated or discontinued by the institution after the completion of the examination.

The purpose of the Community Reinvestment Act of 1977 (12 U. S. C. 2901), as amended, is to encourage each financial institution to help meet the credit needs of the communities in which it operates. The Act requires that in connection with its examination of a financial institution, each federal financial supervisory agency shall (1) assess the institution's record of helping to meet the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operations of the institution, and (2) take that record of performance into account when deciding whether to approve an application of the institution for a deposit facility.

The Financial Institutions Reform, Recovery and Enforcement Act of 1989, Pub. L. No. 101-73, amended the CRA to require the Agencies to make public certain portions of their CRA performance assessments of financial institutions.

Basis for the Rating

The assessment of the institution's record takes into account its financial capacity and size, legal impediments and local economic conditions and demographics, including the competitive environment in which it operates. Assessing the CRA performance is a process that does not rely on absolute standards. Institutions are not required to adopt specific activities, nor to offer specific types or amounts of credit. Each institution has considerable flexibility in determining how it can best help to meet the credit needs of its entire community. In that light, evaluations are based on a review of 12 assessment factors, which are grouped together under 5 performance categories, as detailed in the following section of this evaluation.

ASSIGNMENT OF RATING

Identification of Ratings

In connection with the assessment of each insured depository institution's CRA performance, a rating is assigned from the following groups:

Outstanding record of meeting community credit needs.

An institution in this group has an outstanding record of, and is a leader in, ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

Satisfactory record of meeting community credit needs.

An institution in this group has a satisfactory record of ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

Needs to improve record of meeting community credit needs.

An institution in this group needs to improve its overall record of ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

Substantial noncompliance in meeting community credit needs.

An institution in this group has a substantially deficient record of ascertaining and helping to meet the credit needs of its entire delineated community, including low- and moderate-income neighborhoods, in a manner consistent with its resources and capabilities.

DISCUSSION OF INSTITUTION'S PERFORMANCE

Institution's Rating:

This institution is rated **outstanding record of meeting community credit needs** based on the findings presented below.

REGULATION BB - COMMUNITY REINVESTMENT ACT

COMMUNITY PROFILE

McHenry State Bank is located in McHenry, Illinois, approximately fifty-five miles northwest of Chicago. In accordance with the provisions of the revised CRA, in November of 1995, the bank redefined and expanded its delineation to conform to political boundaries and to encompass four census tracts which were only partially encompassed by the bank's former delineation (a seven-mile radius of the bank's main office in McHenry). The bank's delineated community can generally be described as a square area including the east central portion of McHenry County and the west central portion of Lake County with the bank's main office in McHenry centrally located in the delineated community. The delineation includes 18 census tracts in the Chicago Metropolitan Statistical Area (MSA) (13 tracts are in McHenry County and five tracts are in Lake County). According to the 1990 U.S. census data, the population within these 18 census tracts is 119,162 with the racial and ethnic demographics as follows: 95.76% White, 0.20% Black, 3.16% Hispanic and 0.27% other minorities. There is one low- and moderate-income census tract (in Fox Lake) and no minority census tracts in the bank's delineated community.

Urban communities and their corresponding populations within the bank's delineated community are Crystal Lake - 28,016 [only the northern portion (two census tracts) is in the bank's delineation], McHenry - 16,177, Woodstock - 14,353, Fox Lake - 7,478 and Wauconda - 6,294. Crystal Lake is the most urbanized area, having a large concentration of retail outlets and various industries with a significant economic impact on the bank's market. Rural communities located in the bank's delineated community with populations less than 6,000 include: Bull Valley, Holiday Hills, Ingleside, Island Lake, Lakemoor, McCullom Lake, McHenry Shores, Oakwood Hills, Pistakee Highlands, Prairie Grove, Richmond, Ringwood, Round Lake, Spring Grove and Wonder Lake.

According to the 1990 U.S. census data, the population of McHenry and Lake Counties is 183,241 and 516,418, respectively. Minorities comprise 5.68% of McHenry County's population and 20.20% of Lake County's population. Discussions with community contacts revealed no measurable concentration of minorities within the bank's delineated community. According to information received from the McHenry County Economic Development Corporation, McHenry County has experienced steady population growth; during the four-year period between 1990 and 1994, McHenry County's population increased approximately 17.8%.

The economy of the McHenry area is primarily dependent upon light manufacturing and the service industry. Community representatives indicated that agricultural businesses are minor contributors to the local economy. According to the 1994 Illinois Manufacturers Directory and information provided by the McHenry County Economic Development Corporation, the major employers and their respective number of employees in the McHenry area are as follows: Centegra Northern Illinois Medical Center, McHenry - 1,700; Intermatic, Spring Grove - 1,150; Precision Twist Drill, Crystal Lake - 900; McHenry County Government Center, Woodstock - 850; Union Special, Huntley - 900; Motorola Cellular, McHenry - 800 (estimate); Brake Parts, McHenry - 770; Graftek Press, Woodstock/Crystal Lake - 700; Sage Products, Crystal Lake - 700; and Follet Library/Software, Crystal Lake/McHenry - 665. One of the most significant recent occurrences that had a positive impact on the economy of McHenry County is the construction of Motorola Cellular's plant in Harvard, located in the northwest portion of McHenry County. According to community representatives, the plant is expected to employ between 3,000 and 5,000 people when fully operational.

According to the Illinois Department of Employment Security as of November, 1995, the unemployment rates for McHenry and Lake Counties were 3.1% and 3.0%, respectively, compared to 4.2% for Illinois and 5.3% for the nation. Employment in McHenry County has continued to improve for the past two years.

According to the 1990 U.S. census data, the median value of a single-family dwelling in the bank's delineated community is \$105,000. According to community contacts, McHenry County has remained the fastest growing county in Illinois with considerable residential construction and business opportunities available. However, land prices are escalating and it is becoming more difficult for families relocating to the area to acquire property in the county.

BANK PROFILE

McHenry State Bank, with total assets of \$446 million as of September 30, 1995, is a subsidiary of Sparbank Incorporated, a one-bank holding company located in McHenry, Illinois. The bank operates its main office and two branches in McHenry, Illinois and a third branch in nearby Johnsburg. In addition, the bank operates five automated teller machines (ATM) all located in McHenry County. The bank is a full-service institution which offers a variety of deposit, loan and trust products [see Assessment Factor (d) for a list of the available loan products].

The bank's primary competitors and their respective locations are: McHenry Savings Bank - McHenry; The First National Bank of McHenry - McHenry; State Bank - Wonder Lake; Home State Bank - Crystal Lake; Amcore Bank N.A. Northwest - Woodstock; and Harris Bank - Woodstock. Local branches of the following institutions also provide competition: LaSalle Cragin Bank FSB - Chicago; St. Paul Federal Bank for Savings - Chicago; and NBD Bank - Wheaton. Other competition is provided by mortgage companies in neighboring Crystal Lake and Fox Lake.

ASSESSMENT OF RECORD

I. ASCERTAINMENT OF COMMUNITY CREDIT NEEDS

Assessment Factor (a) - Activities conducted by the institution to ascertain the credit needs of its community, including the extent of the institution's efforts to communicate with members of its community regarding the credit services being provided by the institution.

Regulatory Expectation

The Statement of the Federal Financial Supervisory Agencies regarding the Community Reinvestment Act (Policy Statement) indicates that an effective CRA process must include methods to ascertain community credit needs on an ongoing basis through outreach efforts to local governments, businesses, and community members and organizations. This ascertainment effort should include a system that facilitates dialogue with these individuals and groups and enables them to communicate their concerns to an officer of the financial institution.

Scope and Findings

The bank's activities, methods for ascertaining community credit needs and efforts to communicate with community representatives were reviewed. These activities included: personal involvement of directors, officers and staff in local groups and organizations; credit needs surveys; officer call reports; direct mailings to targeted groups and a community advisory board.

Bank representatives are also involved in the following groups and organizations, where their personal involvement assists the bank in the ascertainment of local credit needs:

- \$ McHenry Area Chamber of Commerce
- \$ Century 21 Referral Network
- \$ McHenry County Association of Realtors
- \$ The Small Business Development Center
- \$ Johnsburg Community Club
- \$ Johnsburg Education Foundation
- \$ Johnsburg Kiwanis
- \$ Community Bankers Association of Illinois
- \$ Fox Lake Volunteer Fire Department
- \$ Habitat for Humanity
- \$ Home of the Sparrow
- \$ Illinois Restaurant Association
- \$ Johnsburg Oldtimers Club
- \$ McHenry County Bankers' Association
- \$ McHenry County Collectors Association
- \$ McHenry Kiwanis
- \$ McHenry Rotary
- \$ McHenry Women in Action
- \$ Northern Illinois Medical Center
- \$ Pioneer Center of McHenry County
- \$ Women in Management

Bank staff participation in the preceding organizations includes serving on various boards and attending meetings regularly. Bank employees are polled annually about their involvement in community organizations, and are encouraged to provide feedback regarding bank services and community credit needs. This activity provides management with continuing opportunities for discussion concerning the community's credit needs. All information received through this activity is communicated to members of the CRA committee who in turn make monthly presentations to the board of directors.

In October of 1994, the bank began distributing a survey entitled "Proudly Reinvesting in Our Community." This is a Bankers Systems, Inc., brochure which asks respondents to answer questions relating to previous lending experience with the bank, advertising and their awareness of the bank's community activities. Suggestions concerning how the bank can better meet the credit or other needs of the community are also solicited. The brochures were distributed as follows:

Statement Stuffers (11/94)	11,000
Handouts at Trade Fair (10/94)	500
Handouts at Home Recreation Show (4/95)	300

In addition, approximately 500 additional brochures were distributed through the officer call program and as lobby take-ones.

Approximately 450 responses (3.6%) to this survey were received. The survey results revealed community concerns about small business loans, flexible loan requirements, low down payment (5%) loan requirements, investment and financial education. The bank has responded to the concern for small business loans by increasing the emphasis on Small Business Administration (SBA) loans in its calling efforts. In response to the need for flexible loan requirements, the bank instructed lending officers to utilize Insured Credit Services whenever appropriate and to consider portfolio loans versus Federal National Mortgage Association (FNMA) mortgages. The bank also participates in and markets the Illinois First Time Home Buyers program, which is available to individuals who have not owned a home in the prior three years. This program offers loans with 5% down. Although no loans have been made under this program, to date, many of the applications generated in response to marketing efforts were eligible for and received loans through existing mortgage products. For results in response to the need for flexible loan requirements and other programs, see Assessment Factor (j). Also, in response to the need for financial and investment education, the bank held free seminars on construction loans and trust services [see discussion under Assessment Factor (I)].

The bank also utilizes an officer call program to ascertain the credit needs of the community and to maintain regular contact with present customers of the bank. Management indicated that heightened competition from other financial institutions is considered a threat to its commercial loan customer base. Therefore, calling efforts have

focused on reinforcing banking relationships by identifying and meeting the needs of existing customers. Calling officers provide additional information to these customers and cross-sell other bank products and services. Calls to prospective customers are made as time permits or when a particular need is identified by bank staff through customer contact and involvement with groups and organizations. Officer call reports are compiled on a monthly basis and reviewed by the president, the head of lending and the CRA officer. A review of the results (November 1994 through December 1995) revealed that a total of 339 calls were conducted. This was an increase of 268% over the number of calls noted in the previous report of examination for the period of June 1993 to November 1994. The calls were distributed as follows:

	<u># of Calls</u>	<u>Percent of Total</u>
Customer Calls	291	86%
Prospect Calls	41	12%
Referral Source Calls	7	2%
 TOTAL	 339	

Referral source calls include contact with: McHenry County Small Business Development Center, National Association for Self-Employed, Retail Merchants Association and Northeast Illinois Cattleman's Association.

The bank conducts an annual letter writing campaign to local civic groups and churches soliciting information regarding local credit needs and offering financial counseling assistance. On May 15, 1995, letters were sent to 46 organizations. Although no new or significant information regarding credit needs has been received through this source to date, one consumer has been referred to the bank for credit counseling as a result of this activity.

The bank has continued to utilize its Community Advisory Board for ascertainment of credit needs; the board is comprised of five community representatives. These members include a corporate president, a pastor, a school district superintendent and two local businesswomen. The chairman and president of the bank periodically attend these meetings. The former president (currently a director) of the bank serves as chairman of this board. The CRA officer also attends meetings regularly and coordinates the bank's responses to committee suggestions. As a direct result of this initiative, the bank has produced a twelve minute video promoting the City of McHenry to new residences and businesses [see Assessment Factor (I)].

Since the previous examination, the bank has added round table luncheons with area realtors as a method of ascertaining credit needs. These sessions are used to discuss current credit needs in the real estate market and available loan programs designed and offered by the bank to meet the needs.

The bank has formed an ongoing relationship with Habitat for Humanity to assist in ascertainment of local housing-related credit needs. The need for low-income housing construction and development has been more clearly defined for the bank through its involvement with this organization. See Assessment Factors (h) and (l) for additional information concerning this initiative.

As a result of information obtained through ascertainment activities, the bank changed its ATM network from Money Network to Cash Station (see Assessment Factor (g)). This was in response to information received from front line employees who indicated that more ATM Cash Stations were available in the Chicago area and suburbs. Similar information was noted in customer responses to the bank's survey.

Conclusions

The bank's ascertainment efforts are varied and spread throughout the entire delineated community. Since the previous examination, ascertainment activities have increased and include participation in Habitat for Humanity, round table discussions with area realtors and emphasis on the officer call program. These additional activities have expanded the existing ascertainment methods into a program which serves as an effective and informative means of determining credit needs throughout the delineated community and communicating these needs to management. The bank responds in a timely manner with appropriate credit products and services to meet identified and changing credit needs.

Assessment Factor (c) - The extent of participation by the institution's board of directors in formulating the institution's policies and reviewing its performance with respect to the purposes of the Community Reinvestment Act.

Regulatory Expectation

The Policy Statement states that banks are encouraged to develop a CRA plan to ensure an affirmative effort on the part of the bank to comply with the Act. It further states that the duty to coordinate and monitor the CRA process should be assigned to a senior officer or a committee charged with the responsibility to report periodically to the board of directors about the bank's CRA efforts, performance, and areas for improvement, where appropriate. An employee training program should be established which addresses information about those policies of the bank designed to help meet community credit needs including the needs of low- and moderate-income areas and small businesses. Procedures should be implemented to ensure that files are maintained, as required by the regulation, for purposes of receiving public comments and for reviewing and responding to the comments.

Regardless of how the bank organizes itself to implement its CRA plan, seeing that the institution has taken the steps necessary to help meet its community's credit needs is the responsibility of the entire organization, beginning with its board of directors and continuing through its line management. To be effective, a CRA plan must include methods to incorporate findings regarding community credit needs into the development of products and services that the bank decides to offer to help meet these needs.

The Policy Statement also states that the bank's CRA statement should accurately reflect the types of lending and other services that the bank is willing to offer to the community. This statement must be reviewed at least annually to ensure its accuracy. The services that the bank chooses to offer should be clearly articulated and reasonably related to community needs.

Scope and Findings

Participation by the board of directors in formulating policy and reviewing the bank's

performance under CRA related activities was reviewed. The following were reviewed to assess the effectiveness of board of directors participation: the bank's written CRA Policy; the January 1995 CRA Action Plan; minutes of the CRA committee meetings; annual CRA self-assessment reports; 1995 and 1994 CRA Statements; the CRA Public File; training activities; and minutes of board of directors meetings.

The bank's CRA Policy was adopted on November 18, 1993, and was recently updated on April 13, 1995. This policy articulates the purpose of CRA and the bank's commitment to meeting the community's credit needs. According to the policy, the bank's CRA program is implemented through an annual CRA Action Plan. The board of directors delegated the CRA officer the responsibility for ensuring that the Action Plan is properly administered. The CRA officer is also required to regularly report the status of the bank's CRA performance to the board of directors. Periodic CRA status reports summarizing CRA efforts and activities are furnished to the board of directors. Analysis of the geographic distribution of approved loans and denied loan applications is also provided to the board of directors.

The bank's 1995 CRA Action Plan was completed and reviewed by the board of directors in January of 1995; it was reaffirmed by the board on April 13, 1995. The 1996 CRA Action Plan is currently under review and is scheduled to be adopted in February of 1996. The 1995 plan categorized the bank's CRA program into five segments: ascertainment, marketing, geographic distribution, illegal credit practices and community development. Each segment details CRA goals and designates responsibilities and methods for effecting compliance with CRA.

The CRA committee meets on a monthly basis; its members includes a representative from the following areas: lending, investments, operations, trust, bank services and compliance. Since the previous examination, a quarterly rotating employee position has been added to the committee. This position is filled by bank employees in positions which entail frequent public contact. The president and past president/community liaison officer represent the board of directors on the CRA committee. The minutes of the CRA committee meetings are reviewed monthly by the board of directors. The CRA officer attends approximately six of these meetings per year.

As part of the CRA program, the bank conducts an annual self-assessment of its CRA performance. A 1994 self-assessment report was completed in December of 1994 and reviewed by the board of directors in January of 1995. More recently, the 1995 self-assessment report was completed and is scheduled to be submitted to the board of directors for review during the February 1996 meeting. A review of these reports revealed a detailed summarization of the bank's annual CRA performance. This information keeps the board apprised of the bank's progress in attaining CRA goals and objectives, as prescribed in the CRA Policy and annual CRA Action Plans.

The board of directors reviews and approves the bank's CRA statement, at least annually, to ensure its accuracy. The most recent review of the CRA statement is evidenced by the minutes of the January 20, 1995 board of directors meeting.

Procedures have been implemented to ensure that files are maintained, as required by the regulation, for purposes of receiving public comments and for reviewing and responding to the comments. A review of the bank's public file revealed that it included all required information. There were no written concerns submitted by community residents.

CRA training is incorporated into the bank's regular training program. The bank also conducts new employee orientation sessions where it provides information regarding credit products, fair lending laws and gives an overview of CRA. See Assessment Factor (f) for additional information on fair lending training.

Conclusions

The directors are active participants in the CRA process. The CRA Policy, adopted by the board of directors, implements a CRA Action Plan. The minutes of the board of directors and CRA committee meetings reflect significant activity and communication on CRA-related issues between the bank and the board of directors. The CRA program is adequate based on the level of involvement by the directors and the comprehensive nature of the CRA training program and the CRA Action Plan.

II. MARKETING AND TYPES OF CREDIT OFFERED AND EXTENDED

Assessment Factor (b) - The extent of the institution's marketing and special credit-related programs to make members of the community aware of the credit services offered by the institution.

Regulatory Expectation

The Policy Statement indicates that an effective CRA plan should include marketing and advertising programs for lending products and services that are responsive to the needs of the community and that will inform and stimulate awareness of those products and services throughout the community, including low- and moderate-income areas.

Scope and Findings

The bank's marketing and advertising efforts, including newspaper, television and other media were reviewed. Community representatives were also interviewed to determine the level of awareness within the community of the bank's products and services.

The bank's marketing efforts are coordinated and monitored by the CRA officer who, as of April, 1995, also serves as the bank's marketing director. The bank marketed its products and services since the previous examination using the media described in the following chart:

Name of Publication	Frequency of Publication	Circulation	Geographic Coverage
Northwest Herald	Daily	33,200 per day	Cities of McHenry, Crystal

Newspapers			Lake, Woodstock and Harvard
Lakeland Newspapers	Weekly	14,400 per week	Primarily Lake County and a small portion of eastern McHenry County
Star Newspapers	Weekly	28,300 per week (Free Publication)	Cities of McHenry, Woodstock, Wonder Lake, Marengo and Harvard
McHenry County Business Journal	Monthly	20,000 per month (Free Publication)	All Businesses in McHenry County
Fifty & Better (Northwest Newspapers, Inc)	Monthly	26,000 per month (Free Publication)	Targets McHenry County consumers Aged Fifty and Older
TCI Chicago Cable Advertising	Daily Cable Television	26,000 Subscribers	Northeast McHenry and Western Lake Counties

The circulation data for the preceding media were compared to demographics of the bank's community and were found to be the primary media within the bank's geographic area. The bank's print advertising budget for 1995 reflects a 63% increase over the 1994 budget. The 1996 proposed print advertising budget reflects an additional 15% increase over 1995. According to bank management, marketing efforts have been expanded since the previous examination to increase product and service awareness in the Fox Lake area, the only low- and moderate-income census tract in the bank's delineated community. This was evidenced in a review of several advertisements placed in the Lakeland Newspapers, the primary media serving this area.

The following chart illustrates the bank's advertising efforts since the previous examination:

ADVERTISING MEDIUM	BANK SERVICES ADVERTISED	FREQUENCY OF ADVERTISEMENTS	PERCENT OF TOTAL BY TYPE
Newspaper	Real Estate	60	34.09%
	Home Improvement	14	7.95%
	Trust/Investment	6	3.41%
	Goodwill	96	54.55%

TCI Chicago Cable Advertising	Real Estate	1,598	32.63%
	Credit Card	148	3.02%
	Club 50	969	19.79%
	Goodwill	2,182	44.56%

Since the previous examination, the bank's marketing emphasis has primarily promoted real estate loan products. In 1995, the bank ran a total of 176 newspaper advertisements with approximately 42% of these advertisements promoting real estate credit products. The bank also ran a total of 4,897 cable television spots with approximately 33% of these advertisements promoting real estate loan credit products. An additional 20% of the televisions advertisements promoted the bank's Club 50 program and the remaining 44% were goodwill announcements. In October of 1995, the bank began advertising in Fifty & Better, a new free monthly publication, which targets approximately 26,000 area consumers aged fifty and older. According to management, area market demographics identify that approximately 30% of the total population is over fifty years of age. There were no advertisements that targeted minorities or which made reference to the bank's bi-lingual employees.

As noted under Assessment Factor (a), the bank's call program expands the overall marketing effort and brings it to a more personal basis. Current information regarding bank rates and lending programs, provided to realtors at round table luncheon meetings, serves to enhance the bank's image in the community.

At the March 27, 1995 Restaurant Trade Show held at the Holiday Inn in Crystal Lake, the bank distributed folders with information on its merchant program and other bank services. A total of six businesses expressed interest in the bank's services.

The following activities were conducted to further support the bank's marketing effort:

On a monthly basis, statement messages which advertised the bank's Classic and Gold Mastercard, and Classic and Gold Visa were sent to approximately 3,700 account holders. In 1995, approximately 37,000 advertisements were sent in this manner.

A coupon for \$50 off closing costs for a home purchase, refinancing or home equity loan was included as a statement stuffer to 12,000 area residents.

In April of 1995, 12,000 stuffers were sent to area residents to promote the bank's Construction Loan and Trust Seminars [see Assessment Factor (l)].

Trust brochures which provide senior citizens and other consumers with information relative to trust and retirement services are available in the bank's public lobby. Other available brochures include: Cash Station Directory, How to Manage Your Checkbook, Solving Debt Problems, Home Affordability Guide, U.S. Savings Bonds for Education, IRAs and Rules for Qualified Retirement Plans.

The following direct mail advertising information was included in the 1995 marketing program:

<u>Advertised Service</u>	<u>Date</u>	<u>Frequency</u>
Automated Teller Services	July 14, 1995	3,961 letters
New Cash Station Services	July 14, 1995	1,495 letters
Club 50/Gold Newsletter	Quarterly	2,600 flyers

The results of community contacts revealed that real estate loan products are the greatest credit need in the community. There were no concerns expressed by community residents relative to the bank's marketing efforts. The results of the bank's survey [as discussed under Assessment Factor (a)] asserted a high level of consumer awareness of the bank's products and services.

Conclusions

The marketing program is considered very strong with the bank expending considerable effort to enhance its image in the community. Advertising is consistent with the community needs as evidenced by the fact that approximately 42% of newsprint advertisements and 32% of televised spots promote real estate loan products, the primary credit need in the community. The total marketing effort creates a strong community awareness of bank products and services, and results in loan originations in the community.

Assessment Factor (i) - The institution's origination of residential mortgage loans, housing rehabilitation loans, home improvement loans, and small business or small farm loans within its community, or the purchase of such loans originated in its community.

Scope and Findings

The distribution of the bank's loan portfolio was analyzed to assess the bank's level of real estate and small business lending. A review of the bank's September 30, 1995 Consolidated Report of Condition revealed a loan-to-deposit ratio of 71.49%. The distribution by loan type was as follows:

LOAN TYPE	DOLLAR AMOUNT OUTSTANDING (000's)	PERCENT OF TOTAL LOANS
REAL ESTATE		
Construction	8,373	3.05
Residential (1-4)	147,113	53.58
Commercial	32,604	11.88
Agricultural	377	0.14
Multi-family	11,798	4.30
CONSUMER		
Open-end Credit	3,227	1.17
All Other	17,307	6.30
COMMERCIAL AND INDUSTRIAL	45,685	16.64
AGRICULTURAL	1,499	0.55
STATE AND POLITICAL OBLIGATIONS	5,595	2.04
OTHER	980	0.35

The loan distribution in the preceding chart was compared with information contained in the previous report of examination (September 30, 1994, Consolidated Report of Condition). The comparison revealed that total loans increased by \$17.2 million (6.70%).

Construction and multi-family real estate loans increased by \$1.6 million (24.61%) and \$4.1 million (54.10%), respectively, while one to four family residential and commercial real estate loans decreased by \$8.4 million (5.41%) and \$6.1 million (15.93%), respectively. In consumer lending, although open-end credit decreased slightly, all other consumer loans increased significantly by \$9.3 million (an increase of 117.80%). Commercial and Industrial loans reflected an increase of \$15.2 million (50.20%). Management attributed the improved loan volume to a strong real estate construction market, an increase in population and the bank's strong marketing effort. Decreases in loan volume were in rate-sensitive refinancings, which appeared to be a reflection of market conditions. Information obtained from area residents also corroborated the bank's observations.

The bank participates in a loan program offered through Insured Credit Services, which enables the bank to originate home equity loans with loan-to-value ratios greater than 80%. This service allows applicants whose loan-to-value ratio exceeds 80% the opportunity to obtain real estate loans with mortgage insurance. In 1995, the bank made 84 loans (totaling \$1,511,204) under this program.

The bank offers bi-weekly payment option mortgage loans which allows some flexibility in meeting special loan requests. In 1995, the bank extended 60 bi-weekly loans totaling \$7,752,600.

At the Home & Recreation Show on April 1 and 2, 1995, the bank offered a below prime rate 8.95% fixed rate home equity rate for five years with no fees. Fifty-one new loans

(totaling \$786,146) were extended in fifteen days as a result of this special program. Although the loans were secured by real estate, loan purposes were varied including motor vehicle purchases, college education, bill consolidation and home improvement. The bank offers a "Patient Loan Program" allowing patients of Northern Illinois Medical Center to obtain a loan to pay for medical expenses not covered by insurance. Since the previous examination, two loans were made totaling \$5,676. There are seven loans outstanding totaling \$10,576.

Conclusions

The bank is primarily a real estate lender although its overall product line is flexible enough to meet the community's changing credit needs. The bank's loan-to-deposit ratio of 71.49% and information received from community contacts suggests that the bank is actively pursuing and originating loans. The bank originates loans consistent with its CRA statement of credits and the community's credit needs. The bank's decision to offer new or modified products demonstrates its commitment to meeting the credit needs of the community.

Assessment Factor (j) - The institution's participation in governmentally insured, guaranteed or subsidized loan programs for housing, small business or small farms.

Scope and Findings

A review of the bank's participation in government loan programs was conducted. Government loan programs in which the bank participates include: Small Business Administration (SBA) Loan Program, Illinois Guaranteed Student Loan Program, Illinois Housing Mortgage Program, Illinois Treasurer Deposit Loan Program and Federal National Mortgage Association (FNMA).

The following chart summarizes the bank's activity in government sponsored loan programs:

PROGRAM	OUTSTANDING		SINCE PREVIOUS EXAMINATION	
	NUMBER	DOLLAR AMOUNT	NUMBER	AMOUNT
SBA	9	\$1,738,152	5	\$361,000
Student Loans *	N/A	N/A	538	\$873,460
Illinois Housing Mortgage Program	2	\$119,708	-0-	-0-
Illinois Treasurer Deposit Program	7	\$635,813	4	\$68,000

*In 1994, the bank sold its student loan portfolio; however, the bank continues to participate in the Sallie Mae Export Loan Program. Student loans are funded and disbursed by the bank and then subsequently purchased and serviced by Sallie Mae.

In addition to the preceding, the bank sells mortgages in the secondary market to FNMA which allows the bank to reinvest funds for new loans. Since the previous examination, the bank has sold 130 "zero point mortgages" loans (totaling \$11,760,800). This

mortgage loan product provides an additional benefit to the local economy in the form of lower closing costs. The bank retains the servicing rights to these loans and presently services approximately 1,000 FNMA loans.

Conclusions

The bank's participation in government loan programs is consistent with the community's need for these types of products. The bank offers and extends a variety of products which provide flexibility in lending and accommodate borrowers who may not have otherwise qualified for loans.

III. GEOGRAPHIC DISTRIBUTION AND RECORD OF OPENING AND CLOSING OFFICES

Regulatory Expectation

Reasonableness of Community Delineation

The regulation requires state member banks to prepare, and at least annually review, a delineation of the local community or communities that comprise its entire community, without excluding low- and moderate-income neighborhoods. Maps are required to be used to portray community delineations. The regulation requires Federal Reserve System examiners to review the reasonableness of the delineations.

The regulation states that a local community shall consist of the contiguous areas surrounding each office or groups of offices, including any low- and moderate-income neighborhoods in those areas. In preparing its delineation, a bank may use any one of the three methods, as stipulated in the regulation: (1) existing boundaries, such as those of a Metropolitan Statistical Area or counties in which the bank's office or offices are located; (2) the bank's effective lending territory, which is defined as that local area or areas where it makes a substantial portion of its loans and all other areas equidistant from its offices; or (3) any other reasonably delineated local area that meets the purposes of CRA and does not exclude low- and moderate-income areas.

Scope and Findings

The distribution of the bank's loans, servicing abilities of its branch system and local market demographics were reviewed to determine the reasonableness of the bank's assessment area.

In November of 1995, in response to encouragements contained in the previous report of examination, the bank adopted a new delineation based on political boundaries (census tracts). This resulted in an expansion of the former delineated community from an area within a seven-mile radius of the bank's main office in McHenry (containing 14 full and four partial census tracts), to an area defined by the outer boundaries of these same 18 contiguous census tracts. The delineation can generally be described as a square area including the east central portion of McHenry County and the west central portion of Lake County with the bank's main office in McHenry centrally located in the delineated community. There is one low- and moderate income census tract and no minority census tracts within the delineated community. The bank has defined its delineated community utilizing method number one described above. The delineated community was reviewed and approved by the board of directors on April 13, 1995 and November 9, 1995.

Conclusions

A review of the examination loan sample [discussed under Assessment Factor (e)],

analysis of the distribution of the bank's loan portfolio as of September 30, 1995, the distribution of the branch offices and local demographics support the reasonableness of the delineation.

Assessment Factor (e) - The geographic distribution of the institution's credit extensions, credit applications and credit denials.

Regulatory Expectation

The Policy Statement states that the services that the bank chooses to offer should be distributed within the bank's community in a fair and nondiscriminatory manner, in keeping with the bank's general approach to its business.

Scope and Findings

The bank's 1993 and 1994 HMDA data, the 1995 preliminary LAR data, the bank's analysis of the geographic distribution of loans and the examination loan sample of recently approved loans and denied credit application were reviewed.

According to the 1994 HMDA data, 80% of the bank's HMDA reportable loan originations were within the delineated community; this is a small decrease from the previous year's figure of 84.1%. The dominant product in 1994 was refinancings, accounting for 59% of total loans made inside the delineation and 54% of total loans made outside the delineation. The bank made 84% of its home improvement loans within its delineation in 1994. Multi-family loans had the highest percentage (45%) of originations outside of the delineation. According to management, this was attributed to the staff's expertise in multi-family lending combined with a low volume of requests for such loans from within the delineated community. Management indicated that single-family residences are most popular within the delineated community, with more multi-family residences being constructed in several communities outside the area. The bank considers all requests for multi-family loans from outside of the delineated community, because opportunities for originating multi-family loans within the community are limited.

The bank's review of its loan portfolio includes: analyzing HMDA data, plotting loan originations on a map, reviewing denied loan applications by census tract, and reviewing its competitors HMDA data. The bank's December, 1995 analysis revealed that 79% of loan originations (both number and dollar amount) were made within the delineation. An observation of the map revealed a reasonable distribution within the delineated community for 1995.

The examination loan sample revealed the following geographic distribution:

LOAN TYPE	TOTAL SAMPLED	WITHIN THE LOCAL DELINEATED COMMUNITY	PERCENT OF TOTAL
Installment	30	25	83.33
Real Estate	21	20	95.24
Single Pay	10	8	80.00
Overdraft	10	9	90.00
Protection			
Credit Cards	10	8	80.00
Total Approved	81	70	86.42

Denials	43	36	83.72
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This review revealed a reasonable distribution among the bank's credit products. At least 80% of all sampled products were originated within the bank's delineated community.

Conclusions

The geographic distribution of the sampled credit applications and loan originations and, the bank's internal analysis of its loans and denied credit applications support the reasonableness of the delineated community. Loans are reasonably distributed throughout the community.

Assessment Factor (g) - The institution's record of opening and closing offices and providing services at offices.

Scope and Findings

The bank's branch closing policy, services available at all four facilities, hours of operation and ATM locations were reviewed.

The bank has a written branch closing policy which was approved by the board of directors on March 18, 1994. The policy outlines branch opening, closing and consolidation procedures. It provides for appropriate notices and review of the impact a closing may have on the community and services to customers. No offices have been opened or closed since the previous examination.

The main bank is located at 3510 West Elm Street, in McHenry. Two branches are also located in McHenry at 1308 North Richmond Road, and 4502 West Crystal Lake Road. A third branch is located in Johnsburg at 3805 Wilmot Road (Johnsburg Building). There are no branches located in low- and moderate-income areas. Only the main bank is considered a full-service branch office. All four of the bank's locations offer drive-up services. Credit applications are available at all offices, however, loan applications are processed at the main bank. All offices with the exception of 1308 North Richmond are closed on Wednesdays; drive-up/walk-up and lobby facilities are available at 1308 North Richmond on Wednesdays and a loan officer is available to assist customers. The bank's normal hours of operation are 9:00am to 5:00pm; banking hours are extended to 6:30pm on Fridays and 12:00 Noon on Saturdays.

Since the previous examination and in response to customers' requests, the bank changed its ATM network from Money Network to Cash Station. All ATMs are full-service and offer deposit, withdrawal, transfer and balance inquiry services.

Conclusions

The bank's facilities provide a sufficient level of service to its entire delineated community.

IV. DISCRIMINATION OR OTHER ILLEGAL CREDIT PRACTICES

Assessment Factor (d) - *Any practices intended to discourage applications for types of credit set forth in the institution's CRA Statement(s).*

Scope and Findings

The bank's loan products and its portfolio of loans were reviewed. Loan officers were interviewed and branch facilities were visited to assess availability of loan products and other services. Members of the community were interviewed, including representatives of protected classes and principals of businesses to determine their perception of the bank's response to the community's credit needs.

The bank's CRA statement indicates that the following types of credit are available to members of its community: real estate, commercial, installment, municipal, credit card, personal reserve account and student loans; letters of credit; participations purchased and sold; and industrial revenue bond financing. The bank's lending is consistent with the types of loans listed in the CRA statement.

Information obtained during loan officer interviews and branch visits did not reveal any concerns regarding possible discouragement of applicants for the loans listed in the CRA statement. Community representatives also did not reveal any concerns relative to the offering and delivery of credit products and services.

Conclusions

The examination sample of approved and denied credit applications revealed that the bank accepts applications for, and originates credit in accordance with its stated policies. The review also demonstrated that the bank originates credit, by general type, consistent with its CRA Statement. Additionally, no practices were detected during the examination that would discourage applications for the types of credit offered by the bank.

Assessment Factor (f) - *Evidence of prohibited discriminatory or other illegal credit practices.*

Scope and Findings

The bank's loan forms, policies and procedures and recently approved consumer and commercial loans, as well as rejected loan applications were reviewed for compliance with the applicable fair housing and fair lending laws and regulations. Loan officers and other community representatives were interviewed.

The bank has adopted a nondiscrimination/fair lending policy. Fair lending training has been incorporated into the bank's ongoing training program. Annually, the bank reviews its home purchase and refinancing loans by income and gender, and the reasons provided to applicants whose credit request was denied for consistency in applying lending standards. The bank also has established a second review committee

for rejected credit applications. Its function is to review each loan denial (consumer, real estate, credit card, personal reserve account, and commercial) prior to notifying the applicant. The committee meets on a weekly basis.

Conclusions

The bank is in compliance with the substantive provisions of the fair housing and fair lending laws, including the Fair Housing Act and the Equal Credit Opportunity Act.

V. COMMUNITY DEVELOPMENT

Assessment Factor (h) - The institution's participation, including investments, in local community development or redevelopment projects or programs.

Scope and Findings

The bank's community development lending, local bond purchases and specific activities related to the development of affordable housing were reviewed. The level of assistance offered to nonprofit groups, government offices and/or local social service agencies serving low- and moderate-income populations was also reviewed.

A review of the bank's community development loans revealed the following noteworthy transactions:

A \$60,000 three-year interest free loan commitment made in February, 1995 to a not-for-profit housing organization for construction of a home.

A \$1,300,000 loan originated in March, 1995, to a housing developer for the development of 62 acres to include 120 single family residential units with lot prices ranging from \$25,000 to \$30,000. The homes to be constructed will range in price from \$130,000 to \$180,000.

A \$500,000 loan originated in April, 1995 for Phase II of a housing development. The lots are priced from \$36,000 to \$42,000.

A \$7,900,000 loan originated in August, 1995 for the development of land in connection to a new manufacturer moving into the area.

A \$3,400,000 loan originated in September, 1995 for construction of an apartment complex.

A \$5,175,000 loan originated in September, 1995 to finance an apartment complex. Forty percent of the 144 one and two bedroom apartments are HUD Section 8 low-income units.

A \$875,000 loan originated in November, 1995 to a local library. Expansion of the library was essential to maintain pace with the increase in the local population growth.

Since the previous examination, the bank originated six loans (totalling \$2,862,500) to local municipalities.

According to community contacts, the most significant credit need in the area is for housing construction. The preceding loans demonstrate that the bank is an active player in this market. These projects include low-income, residential real estate, multifamily and commercial financing support for the real estate industry.

Conclusions

The bank's community development activities are excellent. The bank is active in several initiatives involving affordable housing and multi-family unit construction. In addition, the bank provides funds for government projects as those opportunities become available. Loans for commercial ventures which assist or promote local community development appear to be an integral part of the bank's lending philosophy.

Assessment Factor (k) - The institution's ability to meet various community credit needs based on its financial condition and size, legal impediments, local economic conditions and other factors.

There are no apparent factors relating to the bank's financial condition and size, or local economic conditions that would prevent the bank from meeting community credit needs.

Assessment Factor (l) - Any other factors that, in the regulatory authority's judgement, reasonably bear upon the credit needs of its entire community.

Scope and Findings

The bank's other programs and services that relate directly to the bank's ability to meet the credit needs of its community were reviewed.

The bank makes substantial monetary contributions in the community. In 1995, the bank donated approximately \$40,000 to area churches and charities and \$42,000 to a local library.

The bank provided area consumers with opportunities to attend Construction Loan Seminars held at the bank on April 27, 1995 and May 11, 1995. Topics such as choosing a lot, loan financing, general contractors and the role of title companies were included in presentations. Approximately 30 couples attended each seminar.

Trust officers presented information on estate planning at a Kiwanis meeting in April of 1995, and in August of 1995. Fifty members of St. Patrick's Ladies Guild attended the meeting.

Since the previous examination, the bank has established contact with Habitat for Humanity, a new low-income housing initiative to McHenry County.

As a result of discussions with its Community Advisory Board, the bank has produced a

twelve minute video which promotes the City of McHenry to new and prospective residents and businesses. Approximately 150 complementary copies of the video were distributed to area realtors, public contact groups and representatives throughout the City of McHenry.

A conference room is made available at the bank at no cost for area groups and organizations seeking a place to hold business or social meetings, seminars and other community gatherings.

The bank offers "no service charge" checking to full-time college students and senior citizens. The bank continues its practice of cashing government checks for all consumers, including those without a banking relationship.

The bank has several bi-lingual employees who are available to speak with consumers in German, French, Ukrainian, Spanish, Persian/Turkish and Italian. One employee has completed a course in beginning sign language.

Conclusions

These additional activities enhance community awareness concerning bank services and promote an attitude of friendliness and approachability that indicates bank staff is available to provide credit services.